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C O N F I D E N T I A L SECTION 01 OF 02 ANKARA 000706

SIPDIS

STATE FOR E, EB AND EUR/SE  
TREASURY FOR U/S TAYLOR AND OASIA - MILLS AND LEICHTER  
NSC FOR EDSON, QUANRUD AND BRYZA  
STATE PASS USTR FOR NOVELLI AND BIRDSEY

E.O. 12958: DECL: 01/28/2008

TAGS: [EFIN](#) [ETRD](#) [PREL](#) [TU](#)

SUBJECT: AMBASSADOR PRESSES DEPUTY PM ON ECONOMIC REFORM,  
RAISES FTA

REF: A. (A) STATE 22328

[1](#)B. (B) STATE 22326

CLASSIFIED BY AMBASSADOR W. ROBERT PEARSON. REASON: 1.5(B, D)

[1](#)1. (C) SUMMARY: Ambassador told Deputy Prime Minister Sener January 28 that Turkey was now seriously off-track on its IMF program, that USG assistance was conditioned on both military cooperation and implementation of the reform program, and that it would be impossible for the USG to agree to assistance until and unless Turkey completed the Fourth IMF review. Ambassador urged the GOT to move quickly to comply with the program and reassure markets. Sener said the government was committed to maintaining macroeconomic balances and, despite difficulties, would meet the primary surplus target of 6.5 percent of GNP. He predicted that the January 28-29 High Planning Council meeting would resolve the budgetary issues for the year. In his view, the January 25 BRSA-Cukurova Group agreement resolves the Pamukbank-Yapi Kredi Bank issue. Noting Tayyip Erdogan's December query about Turkey joining NAFTA, Ambassador asked for clarification on whether the GOT would be able and willing to (a) obtain EU approval for an FTA, and (b) include all sectors, including agriculture, in such a trade agreement. Sener said a possible FTA was "very important," and promised to have his experts study the Ambassador's questions. End Summary.

#### Economic Reform

[1](#)2. (C) Ambassador called on Deputy Prime Minister Abdullatif Sener January 28 to deliver ref A points. He said the USG was very concerned that Turkey was now seriously off-track on its reform program. After the elections, the U.S. had expressed its willingness to offer assistance to Turkey in the event of an Iraq operation, but had made clear that any assistance would be conditioned on Turkey's full implementation of economic reforms and its full cooperation on Iraq. It would not be possible for the U.S. to agree to this assistance until Turkey completed its fourth review under the IMF program. The key issues for that review include achieving the 6.5 percent primary surplus target and resolving the Pamukbank-Yapi Kredi Bank issue. Looking further ahead, it will not be possible for the Administration to win Congressional approval for the assistance package unless Turkey is on-track on the reform program.

[1](#)3. (C) Ambassador added that we understood the draft LOI that Turkish authorities had submitted to the IMF on January 22 was not sufficient; Fund staff had many difficulties with it. At the same time, markets, which had given the new government a vote of confidence after the elections, were now questioning the government's policy direction. Everyone -- the USG, the IMF, and the markets -- want to see good, strong, tough measures to convince the markets the government was committed to reform. Time is limited, so it is important for the government to announce measures quickly that demonstrate this commitment.

[1](#)4. (C) Sener agreed that implementing the economic program was important. The government, he said, was not just looking one year ahead. It would face elections again in four years, and would have to answer to voters then. Government leaders were aware that, if they created macroeconomic imbalances, they would not be able to deliver a sound economy in four years. From this year on, the GOT has to reduce expenditures and increase revenues to maintain macro balances.

[1](#)5. (C) Sener acknowledged that budgetary discussions raised serious issues. For example, they are looking at cutting public investments. This is difficult, particularly because

some projects in the provinces are already underway. Despite these difficulties, Sener insisted that "we will meet the 6.5 percent primary surplus target." He predicted that the High Planning Council meeting, which would begin an hour after his meeting with the Ambassador and continue the next day, would resolve the budgetary issues.

16. (C) On banking, Sener recounted how the IMF had asked him to intervene in the Pamukbank-Yapi Kredi Bank issue, and he had declined. That had turned out to be the right decision, as BRSA and the Cukurova Group reached agreement last weekend on the banks. Under the agreement, the Cukurova Group will withdraw its lawsuit and pull out of the banking sector, while paying off its debts over time. Sener said he considers the issue resolved.

17. (C) Sener said he knew that Treasury had submitted a draft LOI to the IMF, but he had not been informed about IMF concerns on that draft. He acknowledged that market sentiment had worsened in the past several weeks, a fact that he attributed to concerns about the fragile state of public finances and a possible military operation against Iraq. In that sense, it was important that any operation be of short duration.

#### Free Trade

18. (C) Drawing on ref B points, Ambassador reminded Sener that Tayyip Erdogan, during his visit to Washington in December 2002, had raised the idea of Turkey joining NAFTA. The USG, he continued, has said many times that it is open to ideas on how to boost bilateral trade, but has also pointed out that the U.S. approach to FTAs is rigorous and comprehensive. Before he could suggest that Washington consider an FTA, he needed to clarify whether Turkey would be prepared to liberalize all sectors, including agriculture, and whether it believed it could do so within the context of its Customs Union agreement with the EU. Ambassador reiterated that he could not commit the USG to pursue an FTA, but thought it would be useful to get Turkey's views on these two questions.

19. (C) Sener responded that a possible FTA was a "very serious issue." He was aware that Tayyip Erdogan had raised the idea in Washington. "I know Mr. Erdogan very well. He thinks such an agreement should be realized." Sener said he would discuss the matter with the Prime Minister and Tayyip Erdogan, and ask experts to start studying the two questions the Ambassador had raised. At a minimum, should the U.S. and Turkey decide to pursue an FTA, Turkey would have to ask the EU for permission to deviate from the Customs Union's common external tariff. This was a very technical matter, so Turkey will form a working group to look into it, after which the two sides can have a more useful conversation.

PEARSON